Sempra Energy

Bernie Orozco
Director
State Governmental Affairs

(916) 492-4244
borozco@sempra.com

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Dr. Alan Lloyd, Chair
California Environmental Protection Agency
1001 I Street
Sacramento, CA 95812-2815

RE: Climate Action Team Report to the Governor and Legislature

Dear Dr. Lloyd:

Sempra Energy appreciates the opportunity to review the December 8, 2005 Draft Report to the Governor prepared by the Climate Action Team (CAT). We believe it is a good summary of the issues that California faces as it looks at strategies to achieve the goals in the Governor's Executive Order. We understand the Governor's desire that California continue its leadership in environmental protection to address the climate change issue, and again wish to express our desire to continue to work with you to develop a sound policy.

We generally support the report's Overarching Recommendations to the Administration and the Legislature. The recommendations from the CAT, including (1) mandatory greenhouse gas (GHG) emissions reporting; (2) a coordinated investment strategy for State funded programs; and (3) credits for early voluntary reductions, present some good ideas that should be explored in more detail. We are also encouraged by the CAT's recognition that any proposed solution must include as many major emission sectors or market sectors as possible to be effective in meeting the Executive Order.

Sempra Energy believes that mandatory climate change emissions reporting is crucial to understanding how best to establish a program to pursue the Governor's goals. Sempra Energy also believes that technology development through industry incentives and a state-funded, coordinated investment strategy is critical to achieve reductions. Finally, the recommendation that ensures business credit for early voluntary action rewards those who have taken proactive steps prior to any mandated program.

Customers of regulated utilities already pay significant public charges for programs that reduce GHG emissions. For 2006 alone, California's electric customers will already be spending $1-2 billion to finance legislative and regulatory public purpose programs, with cost obligations increasing every year. These programs include the Public Utilities Commission's recent solar programs that ultimately will cost customers of a regulated utility nearly $3 billion while customers of local publicly-owned utilities are not subject to the same requirement. Customers of regulated utilities should not solely bear the costs for GHG reductions while others are allowed to avoid responsibility. Proper implementation of a GHG program should include reasonable responsibility for all industries. Mitigation measures to reduce GHGs from petroleum products, which account for 40% of California's total emissions, should be implemented.

Within the General Recommendations of the Report, Sempra Energy feels strongly that the Climate Action Team must subject any proposed regulations to a full and detailed peer-reviewed economic analysis for cost effectiveness, and for specific macroeconomic impacts to California's citizens and businesses. As the Report points out, "Further assessment is also needed to evaluate the economic implications of a cap and trade program for the state as well as other implementation options."

With regard to the discussion on cap and trade, we wish to draw your attention to the more lengthy comments that we provided to you on December 5, 2005, under my signature. Although the Report touches on many questions to address before considering a cap and trade program for California, it clearly states that "the added benefit and impact of the State taking unilateral action must be assessed." Sempra Energy feels strongly that a unilateral cap and trade program for California would be very difficult to implement, impossible to verify, and would create economic distortions and market issues for the State. The Report concludes that, "The legislative authority required to implement a cap and trade program should be identified." Sempra Energy feels that until California can answer the crucial questions that stand in the way of an effective cap and trade program, it is premature to consider legislative authority for such a program.

Also included in the Report's General Recommendations and in the Cap and Trade Program Design Options Report, is a cursory analysis of allowance distribution mechanisms (i.e., allocation or auction). The Report concludes that, "Both approaches can result in essentially the same cost of controlling emissions, and both approaches are expected to have the same impact on consumer prices in most cases." Sempra Energy feels that the economic impact of an allowance auction could be significant and detrimental to emissions reduction investment opportunities for California's businesses. We feel this topic has not been fully considered and we recommend further study including peer-reviewed modeling assessment of allocation methodologies which can best incent California businesses to reduce greenhouse gas emissions.

Without additional information regarding the assumptions made in the preparation of the Economic Assessment, we find it difficult to evaluate. However, with respect to the renewables conclusion, it appears to rely on a CEC forecast that is inconsistent with forecasts made by others, and relies on the presence of very high natural gas prices. If, as many predict, the access to new supplies brings the cost of natural gas down, then renewables will not compare favorably on a cost basis to natural gas options. If a cap and trade program is implemented, since there are not technologies that can be used to reduce GHG from current operations, offsets would be the only economic option to meeting the goals. In this situation, the cost of acquisition of those offsets would again flow out of California, further burdening its citizens and disadvantaging California's competitiveness. Without a better understanding of what assumptions have been used in the Assessment, however, we can only express concern about its conclusions.

Sempra Energy supports broad-based national programs for GHGs with equitable goals across all market sectors. But, as stated, Sempra Energy is very concerned that an attempt by California to create its own such program needs to be carefully analyzed from both an energy and an economic perspective. A program to pursue the Governor's GHG reduction goals is sweeping in scope and could either enhance California's leadership in innovative energy and environmental technology, or have drastic impacts upon its economy. Let's work together to take action that makes sense for California.

Should you have any questions regarding this issue or the comments that we previously provided, please feel free to contact me or Michael Murray at (619) 696-2320.

Sincerely,

Bernie Orozco

c: Eileen Tutt